
STATUTORY REVIEW OF
ELECTRONIC TRANSACTION FEE PROCESSES

A REPORT TO THE
EXECUTIVE APPROPRIATIONS COMMITTEE

OFFICE OF THE LEGISLATIVE FISCAL ANALYST
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STATUTORY REVIEW OF ELECTRONIC TRANSACTION FEE PROCESSES**SUMMARY**

Revenue Procedures and Control Act Amendments (S.B. 175, 2003 General Session) created new financial procedures through which state agencies handle electronic transactions. The bill requires the Legislative Fiscal Analyst (LFA) to review the new procedures and present a report to the Legislature during the 2006 interim. While the act provided a necessary and useful transition mechanism for enabling online transactions, the LFA recommends allowing the bill to sunset whereby incorporating electronic payment fees into the regular budget process. Prior to the bill's repeal, LFA believes that the Legislature should adjust existing electronic payment surcharges so that they break even; and that appropriators should take action to eliminate non-lapsing dedicated credit balances related to electronic payment fees.

BACKGROUND

During the 2003 General Session, the Legislature passed Senate Bill 175, *Revenue Procedures and Control Act Amendments*. In the bill, legislators primarily authorized state agencies to establish surcharges to cover the cost of electronic payments. They defined electronic payments as "any form of payment processed through electronic means, including credit cards, debit cards, and automatic clearinghouse transactions" (S.B. 175, 2003 General Session, p. 4).

SB 175 authorized state agencies to adjust fees to cover the cost of electronic transactions

An underlying tenet of S.B. 175 is that agencies should not charge separate convenience fees for on-line transactions. With two exceptions, S.B. 175 required agencies to incorporate electronic payment surcharges into established base fees and allowed agencies to raise base fees to cover the incremental cost of electronic payments. The bill's first exception allowed agencies to establish a separate electronic payment fee when a base fee was written in statute and therefore could not be altered administratively. Its second exception allowed the Division of Finance to waive the requirements of the act for agencies that already have an electronic transactions fee and for which complying with the act would be "unduly burdensome".

S.B. 175 also directed the state's Division of Finance to create new revenue and expenditure categories for electronic payment fees and costs. It then required agencies to use such mechanisms to track electronic payment fee revenues and expenditures, whether the fees were separate from or a component of existing fees.

SB 175 directed the LFA to analyze implementation of the bill and make recommendations

The act waives certain provisions of the Revenue Procedures and Control Act for electronic payment fees. The fees are not subject to a 125% cap on expenditures as are other dedicated credits revenues. Further, authority to spend the fee revenue does not lapse at the end of a fiscal year.

Finally, S.B. 125 required the Office of the Legislative Fiscal Analyst to review the provisions of S.B. 175 and report to the Legislature prior to November 1, 2006. Specifically, the bill directed LFA to analyze:

- Whether electronic transaction fees should remain a separate revenue category or be incorporated into base budgets;
- Whether the provisions of S.B. 175 should be continued, modified, or sunsetted; and,
- Whether electronic payment fees should continue to be funded with dedicated credits.

NOT ALL AGENCIES TRACK ELECTRONIC PAYMENT FEES

Only Tax, Commerce, and Insurance track electronic payment fee revenue as required by S.B. 175

The first thing LFA discovered in its review of electronic payment fees is that only three agencies are tracking the fees as directed by S.B. 175. The state Division of Finance reports that only the Utah State Tax Commission, Department of Commerce and Department of Insurance show collections in the special revenue categories developed by Finance under 63-38a-105(6).

It is clear from a visit to the State's web site that other agencies are processing electronic payments. For example, the Department of Natural Resources (DNR) allows its customers to buy hunting and fishing licenses and make park reservations on-line. The Department of Health offers birth certificates, death certificates, and marriage licenses on-line. The Utah Travel Council sells maps, books, and posters on-line. All of these cases, and more, require some sort of electronic credit card or debit card payment, and all must have an associated electronic payment cost.

Agencies that pay electronic payment costs with fee revenue but do not report it to Finance may not be in compliance with S.B. 175

Agencies other than Tax, Commerce, and Insurance may not track electronic payments for a number of reasons. In some cases, agencies state that they have not established specific surcharges for electronic payments and thus are not subject to S.B. 175. Even if those agencies' fees have changed since passage of S.B. 175, the fee changes were not specifically for electronic payments, and thus agencies argue they do not need to be tracked separately as required by S.B. 175.

Depending upon one's reading of S.B. 175, agencies that offer electronic payment of established fees and pay costs associated with those payments but do not track the electronic payment fees in FINET (the state's financial system) may not be complying with state law. UCA 63-38a-106(10) states "After July 1, 2004, an agency may not charge, assess, or establish any fee, convenience fee, or surcharge to cover the cost of electronic payments except as provided in this section." One interpretation of that paragraph is that if agencies charge a fee and part of the revenue from that fee pays for electronic payment costs, that agency must comply with the financial accounting procedures established by S.B. 175, even if electronic payment costs are paid "within base budgets."

Agencies may contract with private vendors who in-turn collect fees whereby circumventing S.B. 175

Other agencies use private sector services to provide on-line transactions. The agencies themselves do not charge an on-line transaction fee. For example, when making an on-line reservation for a state campground, customers pay the standard use fee but are also charged an additional \$8 by on-line application provider ReserveAmerica. Similarly, the Department of Health directs users to two private on-line vendors for death and marriage certificates

at an additional cost. As these fees are not charged by DNR or Health, the departments do not track them as electronic payments in the state's financial system.

EXCESS ELECTRONIC PAYMENT FEES HAVE ACCUMULATED

The three agencies that do track electronic payment fees as directed by S.B. 175 have charged significantly more, on the whole, than they have had to pay. In the first two years of the bill's implementation, Insurance accrued \$68,000 in non-lapsing balances, Commerce accumulated \$532,000, and Tax amassed \$2.4 million. The nonlapsing balances represent electronic payment fees charged to citizens that are in excess of the actual costs associated with the those transactions. Such balances are authorized under S.B. 175.

Agencies charged nearly \$3 million more for electronic payments than they paid in the first two years after S.B. 175

Figure 1 below shows the status of nonlapsing electronic payment fee balances since passage of S.B. 175.

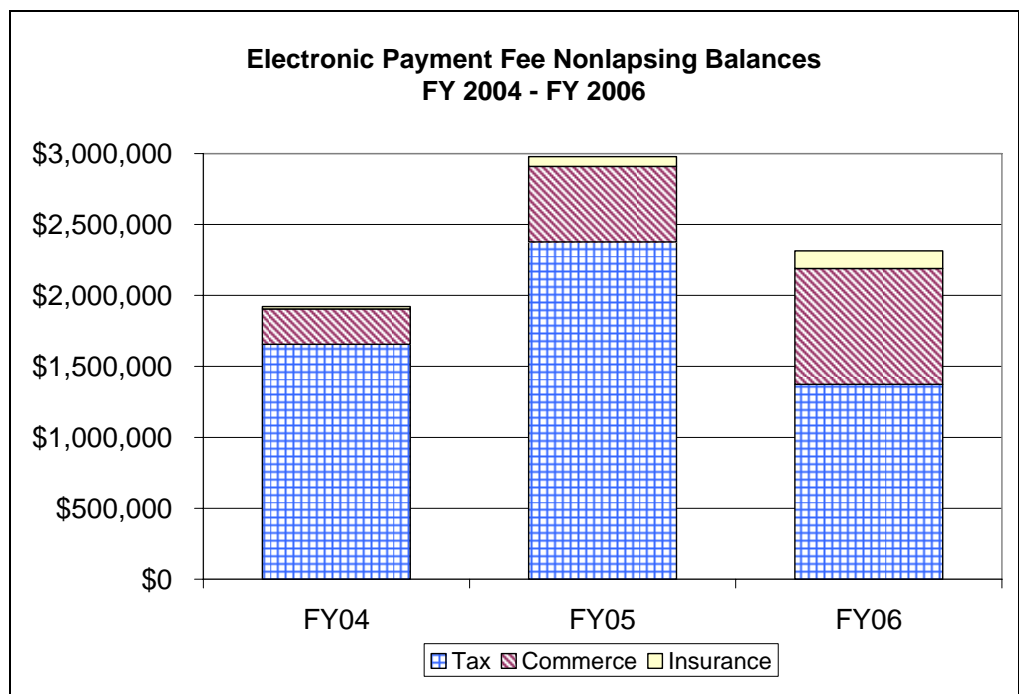


Figure 1

Recognizing the growing balances in electronic payment fee accounts, the Utah State Tax Commission requested a temporary fee reduction beginning in FY 2006. Tax reduced its fee for motor vehicle registration from \$2.00 per transaction to \$0.50 per transaction for FY 2006 and FY 2007. It did so to under-recover electronic payment costs and draw-down balances (See FY 2006 bar in Figure 1). Tax plans to raise its fee to \$1.25 per transaction once balances are depleted.

One agency has already reduced its fees; another plans to do so in the future, and the third wants to use extra fee revenue to offset other on-line costs

The Department of Commerce reports that it plans to reduce many of its electronic payment fees by \$1 beginning in FY 2008. It must seek authorization from the Legislature for such a change during the 2007 General Session.

The Insurance Department would like to use electronic payment balances, as well as ongoing excess fee revenue, to offset other on-line costs. For example, on-line insurance filers pay an \$8 registration fee to a private application service provider in addition to the electronic payment fee charged by Insurance. The Department plans to request authority to partially offset this \$8 fee with surplus from their electronic payment surcharge.

AT LEAST ONE AGENCY COVERS ELECTRONIC PAYMENT COSTS WITHIN BASE BUDGETS

As noted above, the Department of Natural Resources offers online payment for hunting and fishing licenses as well as park reservations. It does so in two ways. For hunting and fishing licenses, it covers electronic payment costs within its base budget. For park reservations, DNR uses a third-party vendor who charges a reservation fee and remits part of the fee to Parks.

DNR is a case study in how electronic payments could be handled absent the provisions of S.B. 175

While the Department may not be in technical compliance with S.B. 175, it has demonstrated that agencies can offer on-line transactions using traditional budget processes. DNR includes electronic transaction costs in its total cost of doing business. It requests from the Legislature under the Budgetary Procedures Act (UCA 63-38-3.2) authority to charge fees based upon those total costs.

DNR's fees for hunting and fishing licenses have changed since implementation of S.B. 175. Many of the fees changed dramatically in FY 2005, and other smaller scale changes occurred in FY 2004 and FY 2007. DNR reports that it has "never explicitly raised fees to cover the cost of electronic payments." Its fees instead have increased due to rising operating costs in general, including rising energy costs, salary increases, and general inflation. In all cases, the fee changes were reviewed and approved by the Legislature.

Practices governed by the Budgetary Procedures Act and Revenue Procedures and Control Act provide accountability for electronic payment fees



Figure 2

Each year the Legislature reviews DNR's nonlapsing balances under UCA 63-38-a-104(2). Unlike balances in the electronic payments accounts, DNR's nonlapsing balances for the two areas discussed in this report – Wildlife and Parks – have decreased or held steady over time. Actual year-end balances for Wildlife and Parks are shown in figures 2 and 3.

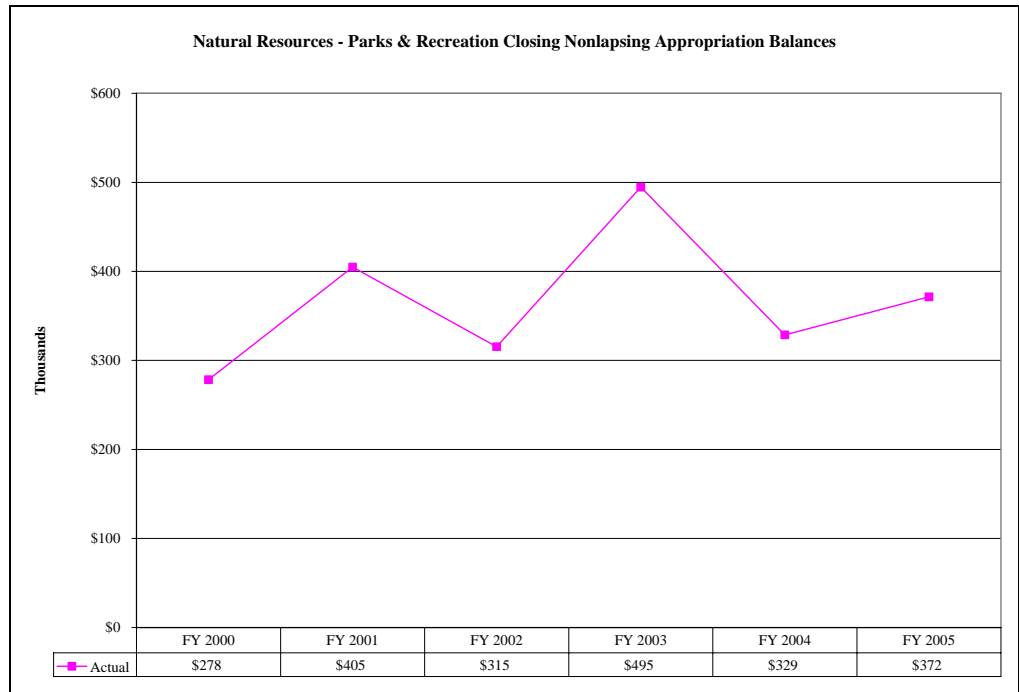


Figure 3

S.B. 175 SHOULD BE ALLOWED TO SUNSET AS CURRENTLY PRESCRIBED BY LAW

LFA believes that S.B. 175 served an essential role in motivating state agencies to offer electronic transactions on-line. It gave explicit authorization for agencies to charge for the cost of electronic payments. It discouraged agencies from establishing separate fees for electronic transaction costs. It jump-started electronic payments by allowing agencies to administratively set fees for one year. S.B. 175 also allowed agencies to gain experience with electronic payment costs and over-time ascertain the correct fees to charge so as to not over-recover.

Recommendation 1

The Office of the Legislative Fiscal Analyst recommends that this sunset provision be left in-force. Utah Code section 63-55b-163 already lists the provisions of S.B. 175 (UCA 63-38a-105) among sections of code that are to be repealed on July 1, 2007.

LFA submits that provisions of the Budgetary Procedures Act govern changes to base fees charged by state agencies and provide sufficient legislative oversight of such fees. The office agrees with S.B. 175 that agencies in general should not charge separate fees for electronic transaction costs, but that those costs should be included in total costs and in-turn reflected in base fees charged to all consumers. LFA recommends that the Legislature and the Governor's Office of Planning and Budget retain a policy discouraging separate electronic payment fees.

LFA further suggests that portions of the Budgetary Procedures Act and the Revenue Procedures and Control Act (outside those in 63-38a-105) provide sufficient accountability for nonlapsing balances. Under these statutes, the Legislature could provide non-lapsing authority through intent language in cases where such authority is warranted.

Recommendation 2 LFA recommends that prior to July 1, 2007 the Legislature and relevant agencies adjust existing fees so that they no longer over-collect for electronic payment costs. In so doing, the Legislature might consider making revenue from the “Electronic Payment Fee for Authorized Motor Vehicle Transactions” – which absent S.B. 175 may be deposited into the Transportation Fund – exempt from statutory limits on the amounts transferred from the Transportation Fund to agencies outside the Utah Department of Transportation (UCA 72-2-103).

Recommendation 3 LFA further recommends that prior to July 1, 2007 the Legislature eliminate existing balances in electronic payment fee dedicated credit accounts by: allowing agencies to draw-down the balances by July 1, 2007; appropriating the balances to agency operating budgets; or lapsing the balances to other relevant funds or fund accounts.

Alternative Should the Legislature decide against repealing S.B. 175 and take action to extend the law, LFA believes that the Office of Legislative Research and General Counsel should review 63-38a-105 and recommend changes that eliminate specific dates that have passed and transition provisions that are no longer relevant.